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IN THE

Supreme Court of the United States

OCTOBER TERM 1956

No. 664

UNITED STATES STEEL CORPORATION,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS.

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OCTOBER TERM 1956.

No. .....

UNITED STATES STEEL CORPORATION,
Petitioner,

v.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS.

Petitioner prays that a Writ of Certiorari issue to review the judgment of the United States Court of Claims, entered on June 5, 1956.

Opinions Below.

The opinions of the United States Court of Claims are not yet officially reported, but are reported in 142 F. Supp. 948 and are printed in Appendix A, *infra*, p. 13.

Jurisdiction.

The judgment below was rendered by the United States Court of Claims on June 5, 1956, and was entered by the Clerk on the same day (R. 39). Petitioner's timely

Motion for Re-Hearing was overruled on October 2, 1956[1] (R. 54). The jurisdiction of this Court is based on 28 U. S. C. §1255(1).

Questions Presented.

1. Is Federal stock issue tax due on the restoration to common stock capital account of an amount previously contained in that account and on which amount Federal stock issue tax previously had been paid?

2. Is Federal stock issue tax due upon a transfer from surplus account to capital account, and, if not, does a subsequent issuance of shares, which itself does not dedicate capital for the first time, attract the tax?

Statutes Involved.

These are:

(1) Section 1800 of the Internal Revenue Code of 1939, Act of February 2, 1939, c. 2, §1800, 53 Stat. 195, 26 U. S. C., 1952 ed., §1800; and

(2) Section 1802 (a) of the Internal Revenue Code of 1939, Act of February 2, 1939, c. 2, §1802 (a) 53 Stat. 196, as amended June 29, 1939, c. 247, §1, 53 Stat. 862, June 25, 1940, c. 419, §209, 54 Stat. 522, September 20, 1941, c. 412, §521 (a) (4), 55 Stat. 707, August 8, 1947, c. 518, 61 Stat. 921, 26 U. S. C., 1952 ed., §1802 (a).

They are printed in Appendix B, *infra*, p. 30.

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[1] The Motion was based on the fact that the Court below drew from the Stipulation of Facts an erroneous inference as to worthlessness of intangibles (R. 54). It seemed the majority opinion had been influenced substantially by this erroneous inference (R. 40, 42, 43, 44, 45).

Statement.

Petitioner brought suit in the United States Court of Claims to recover Federal stock issue tax paid (R. 1). The jurisdiction of that Court was based on 28 U. S. C. §1491. The following facts were before the Court:

1. Between the years 1901 and 1931 petitioner, a corporation organized and existing under the Laws of the State of New Jersey, issued a total of 8,703,252 shares of common stock, having a par value of $100 per share, or a total par value of $870,325,200. Federal stock issue tax was paid on this total amount under the statutes in force at the times of the various issuances. The consideration received for certain of the stock so issued during 1929-1931 exceeded the par value of the stock by $81,250,021.42, and this excess was recorded as capital surplus (R. 15, 16, 17, 18).

2. In 1938 petitioner altered its common stock from par value of $100 per share to no par value with a stated value of $75 per share. This resulted in a reduction of $217,581,300 in stated value of common stock. The amount of this reduction was credited to the capital surplus account, thereby increasing that account to $298,831,321.42 (R. 18).

3. As of December 31, 1938 the recorded value of petitioner's intangible assets, previously carried on the books at a value of $260,368,521.53, was written down to one dollar. The amount of the reduction, $260,368,520.53, was charged to capital surplus, reducing the amount of capital surplus to $38,462,800.89 (R. 18).

4. At a meeting of petitioner's Board of Directors on January 25, 1949 a resolution was adopted to transfer, as of December 31, 1948, $38,462,801 from capital surplus to common stock capital account and $179,118,499 from earned surplus to common stock

capital account, or a total of $217,581,300. Such transfers to common stock capital account were to increase the stated capital in respect to issued and outstanding shares of common stock from $652,743,900 to $870,325,200, the latter amount being equivalent to $100 per share for each of the 8,703,252 shares of no par value common stock then outstanding. Pursuant to such authorization, as of December 31, 1948 petitioner on its books charged $38,462,800.89 to capital surplus account, eliminating the balance in that account, and charged $179,118,499.11 to earned surplus account, and credited the aggregate of $217,581,300 to common stock capital account, increasing that account from $652,743,900 to $870,325,200, the amount in that account before the reduction in 1938, and being an amount on which stock issue tax already had been paid (R. 19).

5. At the same meeting of the Board of Directors of petitioner, resolutions were adopted declaring it advisable to split the common stock of petitioner three for one, by changing each share without par value into three shares without par value; and to change the stated value of the common stock from $100 per share to $33⅓ per share; and to submit the proposal to the annual meeting of stockholders to be held May 2, 1949. At the annual meeting, which was the first meeting of stockholders subsequent to the meeting of the Board of Directors held January 25, 1949, the action proposed at the Directors' meeting was voted (R. 19, 20).

6. Pursuant to such action of the directors and stockholders, the Certificate of Incorporation of petitioner was duly amended, and upon the taking effect of the amendment each share of common stock, without par value, outstanding immediately before the amendment was changed and reclassified into three shares of common stock, without par value. Each certificate representing one or more shares of common stock which were issued and outstanding immediately

prior to the taking effect of the amendment upon the taking effect of the amendment represented the same number of shares, and such certificates remained outstanding, and in June 1949 the petitioner issued to stockholders of record at the close of business on May 12, 1949 in respect to each share of common stock then held of record certificates representing two additional shares of common stock. The common stock capital account as of December 31, 1948, of $870,325,200 remained unchanged (R. 20, 21).

The Court of Claims held that of the total amount of $217,581,300 by which petitioner's common stock capital account was increased as of December 31, 1948, $28,005,050.41 was an amount previously dedicated as capital, and no Federal stock issue tax was due with respect to that amount, and the balance of $189,576,249.59 was an amount dedicated as capital for the first time, and therefore Federal stock issue tax was due with respect to that amount (R. 46). The Court of Claims accordingly allowed a refund of tax paid of $30,805.67 and entered judgment for that amount with interest as allowed by law[2] (R. 55).

Reasons for Granting the Writ.

1. The decision of the Court of Claims conflicts with the decision of the Court of Appeals for the Seventh Circuit in *United States* v. *Pure Oil Co.*, 135 F. 2d 578 (1943).

In the *Pure Oil* case shares of preferred stock with dividend arrearages had been exchanged for an equal number of shares of new preferred stock plus additional shares of

[2] The judgment entered failed to allow refund of related assessed interest paid of $3,295.08. Petitioner has moved to amend the judgment accordingly and the Government has consented to the amendment, but the Court below has not yet acted on the motion (R. 56).

stock in satisfaction of the unpaid dividends. The Treasury asserted stock issue tax not merely on the additional shares but on the entire issue. To justify its position the Treasury argued that the entries on the corporate books failed to show which of the new shares had been substituted for the old shares, and were thus chargeable against capital, and which of the new shares were chargeable against surplus in satisfaction of the dividend arrearages. The Court held that only the net increase in capital was subject to Federal stock issue tax and that the formal bookkeeping entries were not determinative, saying (pp. 579, 580):

> "But book entries alone are not decisive. *Rio Grande Oil Company* v. *Welch*, 9 Cir., 101 F. 2d 454. • • • Whatever the book entries, the only new thing that could properly have gone into the capital account was the contribution by the shareholders of their unpaid dividends to the corporation in consideration of which they received the additional shares."

The Court below, holding to the contrary, found that petitioner's book entries *were* decisive in determining taxability. Prior to 1938 petitioner had issued $100 par value per share common stock with a total par value of $870,325,200. Stock issue tax had been paid on that total par value. In 1938, when this stock was changed to no-par stock with a stated value of $75 per share, the amount of the reduction, $217,581,300, was recorded as capital surplus, increasing the amount recorded in that account to $298,831,321.42. Thereafter in 1938 petitioner decided to write down the recorded value of its intangible assets from $260,368,521.53 to one dollar, and as a matter of bookkeeping petitioner charged its capital surplus account with the difference of $260,368,520.53, leaving $38,462,800.89 as the recorded amount of capital surplus. When petitioner, as of December 31, 1948, increased the stated value of

the stock to $100 per share, thus restoring the amount of $217,581,300 to the common stock capital account, $38,462,800.89 of the restoration was charged to the capital surplus account and $179,118,499.11 was charged to earned surplus.

The Court of Claims held that, as a result of the book entries made when the value of the intangible assets was written down in 1938, it was impossible *to identify* as an amount previously dedicated as capital $189,576,249.59 of the amount restored to the common stock capital account in 1948.[3]

The conflict between the decision below and the decision of the Seventh Circuit in the *Pure Oil* case on the question of whether, for this purpose, book entries are controlling is clearly demonstrated in the following language from Judge Laramore's dissenting opinion below:

> "I respectfully dissent because I believe the majority opinion is contrary to the plain terms of the statute, and it bases the Federal stock issue tax solely on bookkeeping entries as such, which have never been considered controlling of any substantive question of tax law. * * *

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[3] Because $81,250,021.42 of the amount of $298,831,321.42 recorded as capital surplus prior to the write-down of the recorded value of the intangibles represented the excess of the consideration received over par value of common stock issued during 1929-1931 (and on which excess, therefore, no stock issue tax had been paid), the Court held that of the amount of $38,462,800.89 transferred from capital surplus to the common stock capital account

$$\frac{\$\ 81,250,021.42}{\$298,831,321.42}, \text{ i.e., } \$10,457,750.48,$$

was subject to tax. Adding that amount to the amount of $179,118,499.11 charged to petitioner's earned surplus account on the restoration to common stock capital account, the Court held that the total amount of $189,576,249.59 was subject to Federal stock issue tax (R. 44, 45).

"The majority opinion holds that the full amount cannot be traced or identified because the accountant charged capital surplus with the write-down of the intangibles instead of earned surplus. The statute does not require the tracing of funds, which is in and of itself an artificial concept, but on the contrary specifically stated that only the 'amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise,' is to be taxed. The clause 'whether by a transfer of earned surplus or otherwise' indicates that Congress was not basing the tax on book entries. I do not believe that Congress ever intended that the tax would be determined on whether the accountant used one surplus theory in keeping the books of the corporation or another. * * * Some of the difficulty that will result from treating bookkeeping entries as controlling taxability is demonstrated by the difficulty the majority opinion has with the $38,462,800.89 balance in the capital surplus account before the rededication."[4]

The history of Section 1802(a) illuminates the importance of the present conflict. At one time the language of Section 1802(a) merely called for the imposition of stock issue tax on "each original issue." For many years the Treasury contended that stock issue tax must be imposed in full on such stock issues as exchanges of par for no-par stock, exchanges of common for preferred stock, and stock splits, in which only part, at most, of each new issue was based on a previously undedicated and untaxed amount of capital. This gave rise to much litigation, including *United*

[4] 142 F. Supp. 948 at pp. 953, 954; R. 46, 48, 49; Appendix A, *infra*, pp. 21, 23.

States v. *Pure Oil Co., supra.*[5] One of the arguments which the Government advanced was that Section 1802(a) required the tracing of specific items on the corporate books to the initial stock issue. As noted, the court rejected this argument in the *Pure Oil* case.

While the Treasury had little success in the courts, corporations which did not wish to litigate the question were forced to accede to the Treasury's demands. In order to rectify the situation, Congress in 1947 added the following proviso to Section 1802(a):

> "Provided further, That where such certificates (or shares where no certificates are issued) are issued in a recapitalization, the tax payable shall be that proportion of the tax computed on such certificates or shares issued in the recapitalization *that the amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise,* bears to the total par value (or actual value if no par stock) of such certificates or shares issued in the recapitalization." [Emphasis added.][6]

Despite the clarity of this language and the reason for its enactment, the Court below held that, in order for an

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[5] See also *Bowers* v. *West Virginia Pulp & Paper Co.*, 297 Fed. 225 (2d Cir. 1924); *Rio Grande Oil Corp.* v. *Welch*, 101 F. 2d 454 (9th Cir. 1939); *Southern Pacific Co.* v. *Berliner*, 176 F. 2d 671 (9th Cir. 1949); *United States* v. *California Electric Power Co.*, 187 F. 2d 313 (9th Cir. 1951); *Crown Cork & Seal Co., Inc.* v. *United States*, 118 Ct. Cls. 156, 94 F. Supp. 117 (1950); *American Laundry Machinery Co.* v. *Dean*, 292 Fed. 620 (S. D. Ohio 1923); *Trumbull Steel Co.* v. *Routzahn*, 292 Fed. 1009 (N. D. Ohio 1923); *Standard Manufacturing Co.* v. *Heiner*, 300 Fed. 252 (W. D. Penna. 1924); *In re Grant-Lees Gear Co.*, 1 F. 2d 393 (N. D. Ohio 1924); *Goodyear Tire & Rubber Co.* v. *United States*, 60 Ct. Cls. 448 (1925); *The Cuba R.R.* v. *United States*, 60 Ct. Cls. 272 (1925); *Crown-Zellerbach Corp.* v. *Anglim*, 109 F. Supp. 514 (N. D. Cal. 1952).

[6] Act of August 8, 1947, c. 518, 61 Stat. 921.

issue to be free of stock issue tax, not only must the *amount* dedicated as capital have been previously dedicated as capital, but also the actual *funds* so dedicated must be traceable, or labeled, by book entries as *funds* previously dedicated. Hence, the Court below not only rejected in effect the decision of the Court of Appeals for the Seventh Circuit in the *Pure Oil* case, but it also overrode the statutory language which Congress inserted to prevent the Treasury from acting in the manner which lead to the great amount of litigation of which that case was an incident.

2. The decision of the Court of Claims conflicts with the decision of the Court of Appeals for the Seventh Circuit in *American Steel Foundries* v. *Sauber*, (not yet officially reported), 56-2 USTC Par. 10,081 (November 27, 1956).

In the *American Steel Foundries* case the taxpayer transferred amounts from its capital surplus and net income employed in the business accounts to its common stock account, thereby increasing the stated value of the common stock. No additional shares were issued. The Government imposed stock issue tax on the amount of the increase. The Seventh Circuit held no tax was due, thus rejecting, in the words of that court, the "government's position * * * that a dedication of an amount from a corporation's surplus accounts to its capital stock account constitutes an issue of shares under §1802(a) regardless of whether such a dedication is accompanied by an increase in the number of shares outstanding or by a physical delivery to the stockholders of new or different certificates."

In the present case, pursuant to the action of petitioner's Board of Directors at their meeting on January 25, 1949, transfers were made as of December 31, 1948 from capital

and earned surplus accounts to capital stock account, thereby increasing the latter to the amount in question.[7] While stockholders of petitioner, at their annual meeting on May 2, 1949, authorized a recapitalization, in the form of a three for one stock split,[8] no action then was taken, and none was necessary, to increase the capital stock account, and by the recapitalization no amount was dedicated as capital for the first time.

Under the express terms of the proviso to §1802(a), added by Congress in 1947, no tax was due in respect to the recapitalization, i.e., the stock split, the statute providing that where shares or certificates are issued in a recapitalization tax shall be payable only in respect to "the amount dedicated as capital for the first time by the recapitalization," and here no amount was dedicated as capital for the first time *by the recapitalization.*

Therefore, if any tax was due in the present case it is by reason of the transfers from capital and earned surplus accounts to capital stock account, as of December 31, 1948, pursuant to the action of the Directors at their meeting on January 25, 1949. But the Seventh Circuit, in the *American Steel Foundries* case, has held that on such a transaction no tax is due. It is, therefore, submitted there is a conflict with the decision of the Seventh Circuit.

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[7] Action which could be, and was, carried out unconditionally pursuant to action by the Directors. N. J. Rev. Stat. §14:8-6.

[8] Action which could be taken only on affirmative two-thirds vote of stockholders. N. J. Rev. Stat. §§14:11-1, 14:11-2.

Conclusion.

For the foregoing reasons, this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

A. Chauncey Newlin,
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Of Counsel
William L. Hearne,
Richard H. Appert,
John A. Garvey, Jr.

December 1956.

Appendix A.

Opinions Below.

IN THE UNITED STATES COURT OF CLAIMS

No. 215–55

(Decided June 5, 1956)

UNITED STATES STEEL CORPORATION *v.* THE UNITED STATES

Mr. RICHARD H. APPERT for plaintiff. Messrs. A. CHAUNCEY NEWLIN, JOHN A. GARVEY, JR., WILLIAM L. HEARNE, and WHITE & CASE were on the brief.

Mr. SHELDON J. GITELMAN, with whom was Mr. Assistant Attorney General H. BRIAN HOLLAND, for defendant. Messrs. ANDREW D. SHARPE and JOHN A. REES were on the brief.

OPINION

WHITAKER, Judge, delivered the opinion of the court:

Plaintiff seeks to recover $264,942.19, which was the total of a Federal documentary stamp tax assessed against plaintiff under sections 1800 and 1802 (a) of the Internal Revenue Code of 1939, as amended, and the interest thereon.

The plaintiff is a corporation organized and existing under the laws of the State of New Jersey. From 1901 to 1931 plaintiff issued a total of 8,703,252 shares of common stock, having a par value of $100 per share, and thereby dedicated to capital the total amount of $870,325,200. This sum was carried on plaintiff's books in an account denominated "Common Stock Capital Account." A Federal stock issue tax was paid in respect to all of the shares issued under the statutes in force at the time of the various issues.

Of the aforementioned shares of common stock issued, 1,587,017 were issued in 1929, 1930, and 1931 for cash and

property having an aggregate book value of $239,951,721.42, or $81,250,021.42 in excess of the par value of such shares. In respect to these shares plaintiff paid a Federal stock issue tax at a rate of 5 cents per $100 of par value in accordance with Schedule A, Title VIII, Revenue Act of 1926, 44 Stat. 99, 101. No tax was paid with respect to the $81,250,021.42 excess, and that amount was placed in the capital surplus account on plaintiff's books, and was not dedicated to capital.

In 1938 the plaintiff changed its common stock from par value of $100 per share to no par value with a stated value of $75 per share. This resulted in a reduction in the stated value of the common stock then outstanding and in the common stock capital account from $870,325,200 to $652,743,900, or a reduction of $217,581,300. This amount was credited to the capital surplus account and, when added to the $81,250,021.42 already in that account, brought the total capital surplus to $298,831,321.42.

Later in 1938, plaintiff decided that some intangible property which had been carried on the books at a value of $260,368,521.53 was almost worthless and this amount was written down to $1.00. The sum of $260,368,520.53 was charged against the capital surplus account, reducing the balance in this account to $38,462,800.89.

After these transactions plaintiff had in its common stock capital account $652,743,900 and in its capital surplus account $38,462,800.89. No changes occurred in these accounts for approximately 10 years.

Then, at a meeting of plaintiff's Board of Directors held on January 25, 1949, the Board resolved to increase the common stock capital account as of December 31, 1948, by $217,581,300 so that each of the no par shares of common stock then outstanding would have a stated value of $100 per share instead of $75 per share. In order to do this in part, all of the amount remaining in the capital surplus account was transferred to the common stock capital account, eliminating the balance of the capital surplus account. But since the capital surplus account had been depleted by the charge-off of $260,368,520.53 for worthless

intangibles in 1938, it was necessary to secure the balance of $179,118,499.11 from the earned surplus account in order to provide the amount needed to increase the stated value of common stock to $100 per share. Thus, $179,118,499.11 was charged against the earned surplus account, $38,462,800.89 was charged against the capital surplus account, and a total of $217,581,300 was credited to the common stock capital account, raising the amount in that account to the desired level.

At the same time the Board also determined that it would be advisable to split the common stock 3 for 1 by changing each share without par value into three shares without par value and to change the stated value of each share of common stock to $33⅓. The stockholders approved of this stock split at the first meeting of the stockholders subsequent to the meeting of the Board of Directors. Pursuant to this action of the Board of Directors and the stockholders, two additional shares of no par common stock were issued for each share outstanding.

Subsequently, a tax was imposed upon plaintiff under sections 1800 and 1802 (a) of the Internal Revenue Code of 1939, as amended. Section 1802 (a) provides that upon an original issue of capital stock a tax shall be imposed as follows:

> (a) *Original Issue.*—On each original issue, whether on organization or reorganization, of shares or certificates of stock, or of profits, or of interests in property or accumulations, by any corporation, or by any investment trust or similar organization (or by any person on behalf of such investment trust or similar organization) holding or dealing in any of the instruments mentioned or described in this subsection or section 1801 (whether or not such investment trust or similar organization constitutes a corporation within the meaning of this title), on each $100 of par or face value or fraction thereof of the certificates issued by such corporation or by such investment trust or similar organization (or of the shares where no certificates were issued), 11 cents:

Provided: That where such shares or certificates are issued without par or face value, the tax shall be 11 cents per share (corporate share, or investment trust or other organization share, as the case may be), unless the actual value is in excess of $100 per share; in which case the tax shall be 11 cents on each $100 of actual value or fraction thereof of such certificates (or of the shares where no certificates were issued), or unless the actual value is less than $100 per share, in which case the tax shall be 3 cents on each $20 of actual value, or fraction thereof, of such certificates (or of the shares where no certificates were issued): *Provided further,* That where such certificates (or shares, where no certificates are issued) are issued in a recapitalization, the tax payable shall be that proportion of the tax computed on such certificates or shares issued in the recapitalization that the amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise, bears to the total par value (or actual value if no par stock) of such certificates or shares issued in the recapitalization. The stamps representing the tax imposed by this subsection shall be attached to the stock books or corresponding records of the organization and not to the certificates issued.

The entire $217,581,300 transferred to the common stock capital account as of December 31, 1948, was considered newly dedicated capital and was taxed under the provisions set out above. Plaintiff paid the tax and the interest thereon, which altogether amounted to $264,942.19. It now seeks to recover this amount.

Plaintiff says that none of the $217,581,300 transferred to the common stock capital account as of December 31, 1948, was an "amount dedicated as capital for the first time" and that, therefore, no tax was due.

From the facts set out above it seems clear that the $179,118,499.11 transferred from the earned surplus account

to the common stock capital account was "an amount dedicated as capital for the first time."

It is plaintiff's contention that if the $260,368,520.53 charged off for worthless intangibles in 1938 had been charged against earned surplus, as it says could have been done, instead of against the capital surplus account, the $179,118,499.11 transferred from the common stock capital account to the capital surplus account in 1938 would still have been in the capital surplus account in 1948, and its retransfer to the common stock capital account would not have been a "dedication [of it] as capital for the first time."

The answer to this is that this was not in fact done, and it was not improper to have done what was done. The capital of the company was represented in part by these intangibles, and when they were ascertained to be worthless, it was proper for them to be charged off against the capital account. At any rate, this was what was done. The amount previously dedicated to capital was reduced, because some of the capital had become worthless. This is the way plaintiff chose to handle the transaction.

Under certain facts it might have been proper to have charged these worthless intangibles to earned surplus, on the theory that they had been consumed in the earning of the surplus; but, under the circumstances of this case, plaintiff thought it proper to charge them against the capital account, instead of the earned surplus account, and we cannot say this was improper.

It is plaintiff's position that where an amount dedicated to capital is properly written off the books, due to a decline in the value of assets, a subsequent addition to capital out of earned surplus will not be "an amount dedicated to capital for the first time" as long as the addition to capital does not exceed the previous reduction. Neither the legislative history nor the cases cited by plaintiff support this position, and we do not believe that Congress intended such a result when it added the 1947 amendment to section 1802 (a) restricting the taxable amount to that "amount dedicated as capital for the first time by the recapitalization."

Prior to the 1947 amendment to section 1802 (a), when new shares of stock were exchanged for shares outstanding and, at the same time, a new amount was added to the capital account, the Treasury attempted, in some instances, to make the stamp tax applicable to both the previously existing capital and the newly added capital. This result was permitted in *Southern Pacific Co.* v. *Berliner,* 176 F. 2d 671 (C. A. 9th), a case arising prior to the 1947 amendment, but decided subsequent thereto, and in other cases. This court, in considering this problem, held that the tax was applicable only to sums newly added to the capital account and not to both the previously existing capital and the newly added capital. *Crown Cork & Seal Company, Inc.,* v. *United States,* 118 C. Cls. 156. Although the *Crown* case arose prior to the 1947 amendment, it was decided subsequent to its enactment, and the court indicated that the 1947 amendment was added to make it clear that, in situations similar to the one then before it, the tax should be applicable only to sums newly added to the capital account.

We believe that this was the purpose of the amendment, i. e., Congress intended to make it clear that an amount already in the capital account should not be taxed a second time when a new amount was added to capital and new shares of stock issued. But the $179,118,499.11 taken out of earned surplus and placed in the capital account in the present case was not an amount already in the capital account. It was an amount added to capital for the first time and was properly taxable, as we held in the *Crown Cork & Seal Company* case, *supra.*

But plaintiff says this is contrary to section 113.23 (e) of Treasury Regulation 71 (1941 ed.), 26 CFR 113.23 (e), which reads as follows:

> * * * A tax is not payable with respect to stock issued in a recapitalization unless the recapitalization results in the dedication of an amount as capital which amount is so dedicated for the first time. Thus, where a corporation transferred an amount from capital to capital surplus in a prior recapitalization, and such corporation in a subsequent or second

> recapitalization transfers such amount from capital surplus to capital under such circumstances that the amount so restored to capital is clearly identifiable, a tax is not payable with respect to the amount so rededicated as capital. However, the tax is payable with respect to a transfer of capital surplus to capital by way of a recapitalization where the amount so transferred had not been previously dedicated as capital.

This position cannot be sustained because the $179,118,499.11 transferred from earned surplus to capital cannot be identified as an amount previously dedicated to capital, because it had never been dedicated to capital. It was an amount in the earned surplus account, and, therefore, available for the payment of dividends, or for any other use, since such use of it would not impair the capital. On the other hand, if it had been dedicated to capital, it would not have been available for the payment of dividends, under the laws of some of the States, at least.

In none of the cases cited by either party was an amount previously dedicated to capital written off the books due to a decline in the value of assets as here. For this reason the cases cited are not controlling in the present situation. Since the $179,118,499.11 transferred from earned surplus to the capital stock account had never been dedicated to capital, and since no tax had ever been imposed upon it, we think that a tax on that amount was properly imposed when such dedication did occur.

There remains the question of the $38,462,800.89 transferred from the capital surplus account to the common stock capital account. This question appears to be a novel one.

Plaintiff says that there would not have been this balance in this account except for the transfer to it of the $217,581,300, which had previously been dedicated as capital, and the tax paid on the certificates issued in respect to it. This would seem to be correct.

But, at the same time, there would not have been this balance in the account except for the $81,250,021.42 pre-

mium paid for stock previously issued. No tax was paid with respect to this $81,250,021.42; nor had it ever been dedicated as capital. It could have been distributed as a dividend at the will of the corporation. A part of it was never set apart as capital, because it was consumed in the worthless intangibles charged off.

The result is that the balance of $38,462,800.89 remaining in the capital surplus account, was made up partly of previously dedicated capital and partly of an undedicated amount. Defendant says that the commingling of a dedicated amount and an undedicated amount in the capital surplus account and the subsequent withdrawal of the $260,368,520.53 from that account for the purpose of writing off worthless intangible assets made it impossible to identify any of the $38,462,800.89 remaining in the account as previously dedicated capital. We do not agree. Of the $298,831,321.42 in the capital surplus account before the withdrawal of the $260,368,520.53 to write off intangibles, $81,250,021.42 had never been dedicated to capital. Of the balance of $38,462,800.89 remaining in the account after the withdrawal, we think that 81,250,021.42/298,831,321.42 of it, or $10,457,750.48, was an undedicated amount.

This makes the total amount "dedicated as capital for the first time," $189,576,249.59, and the Government properly assessed a stamp tax on this amount.

Plaintiff also seeks to recover on the theory that the dedication of capital as of December 31, 1948, and the issuance of stock in June 1949 were separate transactions, neither of which was subject to a tax when occurring alone. We agree that both of these elements are necessary before a tax may be imposed under section 1802 (a). However, they were in reality parts of a single plan originating at the meeting of the Board of Directors on January 25, 1949, and should be so considered. And even if they should be considered as separate transactions, it would not change the result. A corporation may transfer part of its surplus to its capital account without then incurring taxable liability if no stock is issued, but if stock is subsequently issued in connection therewith, the amount transferred is then taxable.

A stamp tax was properly assessed by the defendant upon $189,576,249.59 which amount was dedicated to capital for the first time. Plaintiff is entitled to recover the difference between what it actually paid and what it should have paid in accordance with this opinion, with interest thereon as provided by law. Judgment will be entered to that effect. The amount of recovery will be determined pursuant to Rule 38 (c).

It is so ordered.

MADDEN, Judge; LITTLETON, Judge; and JONES, Chief Judge, concur.

LARAMORE, Judge, dissenting:

I respectfully dissent because I believe the majority opinion is contrary to the plain terms of the statute, and it bases the Federal stock issue tax solely on bookkeeping entries as such, which have never been considered controlling of any substantive question of tax law.

During the years 1901 to 1931 plaintiff issued 8,703,252 shares of common stock, having a par value of $100 per share, and thereby dedicated to capital the total amount of $870,325,200. Federal stock issue tax was paid on this amount. In 1938 plaintiff changed these shares from $100 par to no par with a stated value of $75 per share. This reduced the common stock capital account by $217,581,300. As of December 31, 1948, the stated value of each share was increased by $25, so that the amount dedicated to capital was again $870,325,200.

The pertinent part of section 1802 (a) provides that a stock issue tax shall be imposed:

> On each original issue, whether on organization or reorganization, of shares or certificates of stock, * * *: *Provided further,* That where such certificates (or shares, where no certificates are issued) are issued in a recapitalization, the tax payable shall be that proportion of the tax computed on such certificates or shares issued in the recapitalization that the amount dedicated as capital for the first time by

> the recapitalization, whether by a transfer of earned surplus or otherwise, bears to the total par value (or actual value if no par stock) of such certificates or shares issued in the recapitalization. * * *

It is seen from the terms of the above provision that the tax is imposed in a recapitalization only on "the amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise." The term "amount" so used in this section means a quantity, a number, and not particular dollars or funds as the majority opinion indicates. For the purpose of this proviso see H. Rept. 969, 80th Congress, 1st session. It seems clear that the reduction of the amount dedicated to capital and the subsequent restoration of the amount of the reduction is a rededication of that amount to capital and not the dedication of that amount for the first time.

Section 113.23 (e) of Treasury Regulation 71, set out in the majority opinion, specifically recognizes that the reduction of the amount dedicated to capital and the subsequent restoration of the amount of the reduction is a rededication of that amount and not a dedication of that amount for the first time, provided the amount can be traced and identified. Thus, as indicated by the regulation, the following example would not result in a tax. The taxpayer reduces the amount dedicated to capital by $100 and credits a separate account called capital surplus, or some other name to identify it, with $100 and debits the capital stock account with $100. Ten years later in a recapitalization the taxpayer decided to again dedicate that $100 amount to capital. It has maintained this $100 credit in a separate account on the corporate books. It then debits this separate account $100 and credits the capital stock account $100. As stated above, no tax is due since there was a rededication *and* the taxpayer has maintained the credit entry of $100 separate on its books.

The only difference between what the regulation allows, as shown by the above example, and the instant case is that plaintiff did not keep its credit entry in a separate account.

In 1938 plaintiff debited its common stock capital account $217,581,300 and credited that amount to account labeled capital surplus, which already had a credit balance of $81,250,021.42, thus bringing the total credit balance to $298,831,321.42. As of December 31, 1948, plaintiff decided to raise its common stock capital account back to the amount of $870,325,200. It debited the capital surplus account $38,462,800.89 eliminating the balance in that account, debited earned surplus account $179,118,499.11, and credited common stock capital account $217,581,300, thus increasing that account to $870,325,200.

The majority opinion holds that the full amount cannot be traced or identified because the accountant charged capital surplus with the writedown of the intangibles instead of earned surplus. The statute does not require the tracing of funds, which is in and of itself an artificial concept, but on the contrary specifically states that only the "amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise," is to be taxed. The clause "whether by a transfer of earned surplus or otherwise" indicates that Congress was not basing the tax on book entries. I do not believe that Congress ever intended that the tax would be determined on whether the accountant used one surplus theory in keeping the books of the corporation or another. Whether an item should be charged to earned surplus, capital surplus, or to some other account, varies from accountant to accountant. There could be found ample authority among accountants for the charging of the intangibles in the instant case to earned surplus rather than to capital surplus. This is especially true where, as in this case, capital surplus was made up of entirely paid-in capital instead of the various and sundry other items that could have been credited to that account. Some of the difficulty that will result from treating bookkeeping entries as controlling taxability is demonstrated by the difficulty the majority opinion has with the $38,462,800.89 balance in the capital surplus account before the rededication.

I would allow the plaintiff to recover the Federal stock issue tax paid on the $217,581,300 because that *amount* had already been subjected to the tax once and the plain term of the statute prohibited its being taxed a second time.

Findings of Fact

The court having considered the evidence, the stipulation of facts entered into between the parties, and the briefs and argument of counsel, makes findings of fact as follows:

1. United States Steel Corporation, the plaintiff (herein called the "Steel Corporation"), is a corporation organized and existing under the laws of the State of New Jersey. It was incorporated in 1901 with an authorized capitalization of $1,100,000,000, consisting of 5,500,000 shares of preferred stock, $100 par value, and 5,500,000 shares of common stock, $100 par value.

2. At the time of its organization, the Steel Corporation as its initial capitalization issued 5,102,811 shares of preferred stock and 5,083,025 shares of common stock. Capital dedicated in respect to such shares of preferred stock amounted to $510,281,100, or $100 par value per share, and capital dedicated in respect to such shares of common stock amounted to $508,302,500, or $100 par value per share.

3. In respect to such shares of preferred and common stocks the Steel Corporation paid Federal stock issue tax at the rate of 5¢ per $100 of par value, being the sum of $255,140.55 in respect to the 5,102,811 shares of preferred stock, and the sum of $254,151.25 in respect to the 5,083,025 shares of common stock. This tax was imposed under Section 6 and Schedule A of the Act of June 3, 1898, as amended by the Act of March 2, 1901 (56th Congress, Session II, Chapter 906). Such tax was repealed by the War Revenue Repeal Act (Act of April 12, 1902), which took effect July 1, 1902.

4. The preferred stock and common stock referred to herein are the only classes of stock the Steel Corporation has ever had. From the time it was issued the terms of the Steel Corporation's preferred stock have never been changed. In 1903 it issued $150,000,000 of its 5% bonds in exchange for $150,000,000 par value of its preferred stock, reducing its preferred stock capital account to $360,281,100. Since then there has been no change in the preferred stock capital account. The Steel Corporation's common stock capital account of $508,302,500, referred to in finding 2, remained unchanged until 1927.

5. In 1927 a 40% stock dividend was declared and paid on the Steel Corporation's common stock, payable in authorized and theretofore unissued stock, one share of common stock, $100 par value, being issued in respect to each 2½ shares of common stock then outstanding. As a result of this stock dividend, there were issued 2,033,210 shares of common stock, par value $100 per share, or a total par value of $203,321,000. This amount was transferred from the Steel Corporation's earned surplus account to its common stock capital account, increasing the latter from $508,302,500 to $711,623,500. In respect to the stock dividend of said 2,033,210 shares of common stock, the Steel Corporation paid, under Schedule A, Title VIII, Revenue Act of 1926, Federal stock issue tax at the rate of 5¢ per $100 of par value, or a total tax of $101,660.50.

6. In 1929 the Steel Corporation issued rights to subscribe to one share of common stock for each seven shares held, at $140 per share. Pursuant to the exercise of such rights it issued for cash 1,016,605 shares of authorized and theretofore unissued common stock, $100 par value, or a total par value of $101,660,500. The issuance of this stock increased the Steel Corporation's common stock capital account from $711,623,500 to $813,284,000. In respect to said 1,016,605 shares of common stock, the Steel Corporation paid, under Schedule A, Title VIII, Revenue Act of 1926, Federal stock issue tax at the rate of 5¢ per $100 of par value, or a total tax of $50,830.25.

7. In 1930 and 1931 the Steel Corporation issued for cash and property a total of 570,412 shares of authorized and theretofore unissued common stock, $100 par value, or a total par value of $57,041,200. The issuance of this stock increased the Steel Corporation's common stock capital account from $813,284,000 to $870,325,200. In respect to said 570,412 shares of common stock, issued in 1930 and 1931, the Steel Corporation paid, under Schedule A, Title VIII, Revenue Act of 1926, Federal stock issue tax at the rate of 5¢ per $100 of par value, or a total tax of $28,520.60.

8. The 1,587,017 shares of common stock issued in 1929, 1930 and 1931, as set out in findings 6 and 7, were issued for cash and property having an aggregate book value of $239,951,721.42, or $81,250,021.42 in excess of the par value of such shares. This excess amount was set up on the books of the Steel Corporation as capital surplus.

9. As of December 31, 1935, the Steel Corporation and subsidiaries transferred from earned surplus to depreciation, depletion and amortization reserves $270,000,000, to cover the estimated economic obsolescence of properties. This amount had been reserved prior to 1927, principally from earned surplus, as management's estimate of the amount of income which had been reinvested in fixed assets.

10. In 1938 the Steel Corporation, by proper corporate action of its directors and stockholders, changed its common stock from par value $100 per share to no par value with a stated value of $75 per share. In respect to the then outstanding 8,703,252 shares of common stock, this resulted in a reduction in stated value of common stock and in common stock capital account from $870,325,200 to $652,743,900, or a reduction of $217,581,300. This amount was credited to capital surplus account and, when added to the amount of $81,250,021.42 already in that account, as set forth in finding 8, increased the Steel Corporation's capital surplus account to $298,831,321.42.

11. In December 1938 the Steel Corporation carried on its books intangible property of itself and subsidiaries at a value of $260,368,521.53. As of December 31, 1938, this amount was written down to $1, and the sum of $260,368,520.53 was charged against capital surplus account on the books of the Steel Corporation, reducing that account to $38,462,800.89.

12. At a meeting of the Board of Directors of the Steel Corporation held on January 25, 1949, a resolution was adopted to restore, as of December 31, 1948, to earned surplus account the sum of $270,000,000, referred to in finding 9. Pursuant to such authorization, as of December 31, 1948, the Steel Corporation on its books charged depreciation reserves $270,000,000 and credited earned surplus account $270,000,000.

13. At the said meeting of the Board of Directors of the Steel Corporation on January 25, 1949, a resolution was adopted to transfer, as of December 31, 1948, $38,462,801 from capital surplus to common stock capital account and $179,118,499 from earned surplus to common stock capital account, or a total of $217,581,300. Such transfers to common stock capital account were to increase the stated capital in respect to issued and outstanding shares of common stock from $652,743,900 to $870,325,200, the latter amount being equivalent to $100 per share for each of the 8,703,252 shares of no par value common stock then outstanding. Pursuant to such authorization, as of December 31, 1948, the Steel Corporation on its books charged $38,462,800.89 to capital surplus account, eliminating the balance in that account, and charged $179,118,499.11 to earned surplus account, and credited the aggregate of $217,581,300 to common stock capital account, increasing that account from $652,743,900 to $870,325,200.

14. At the said meeting of the Board of Directors of the Steel Corporation on January 25, 1949, resolutions were adopted declaring it advisable to split the common stock of

the Steel Corporation 3 for 1 by changing each share without par value into three shares without par value, thereby increasing the outstanding number of shares of common stock from 8,703,252 to 26,109,756; and to change the stated value of the common stock from $100 per share to $33⅓ per share; and to amend the By-Laws to increase the number of votes which the holders of preferred stock are entitled from one to three votes for each share; and to submit such proposals to the stockholders at the annual meeting of the stockholders to be held May 2, 1949.

15. The annual meeting of the stockholders of the Steel Corporation was held on May 2, 1949, and at that meeting the action proposed at the meeting of the Board of Directors of January 25, 1949, with respect to splitting the common stock, changing the stated value per share of the common stock, and increasing the voting rights of the preferred stock, was approved. The stockholders' meeting of May 2, 1949, was the first meeting of stockholders subsequent to the meeting of directors of January 25, 1949.

16. Pursuant to such action of the directors and stockholders, the Certificate of Incorporation of the Steel Corporation was duly amended, and upon the taking effect of the amendment each share of common stock, without par value, outstanding immediately before the amendment was changed and reclassified into three shares of common stock, without par value. Each certificate representing one or more shares of common stock which were issued and outstanding immediately prior to the taking effect of the amendment, upon the taking effect of the amendment represented the same number of shares, and such certificates remained outstanding, and in June 1949 the Steel Corporation issued to stockholders of record at the close of business on May 12, 1949, in respect to each share of common stock then held of record certificates representing two additional shares of common stock. The common stock capital account as of December 31, 1948, of $870,325,200, referred to in paragraph

13, remained unchanged through December 31, 1951, and thereafter through December 31, 1953.

17. Subsequent to the issuance of the stock certificates referred to in finding 16, a Federal documentary stamp tax was assessed against plaintiff in the sum of $239,339.43. Plaintiff paid the assessment and interest in the sum of $25,602.76. The assessment was based upon sections 1800 and 1802 (a) of the Internal Revenue Code of 1939, as amended.

Conclusion of Law.

Upon the foregoing findings of fact, which are made a part of the judgment herein, the court concludes that as a matter of law the plaintiff is entitled to recover, with interest as provided by law. Judgment will be entered to this effect. The amount of recovery will be determined pursuant to Rule 38 (c).

Appendix B.

Statutes Involved.

Internal Revenue Code of 1939:

Section 1800. Imposition of Tax.

> There shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in Sections 1801 to 1807, inclusive, or for or in respect of the vellum, parchment, or paper upon which such instruments, matters, or things, or any of them, are written or printed, the several taxes specified in such sections.

Section 1802. Capital Stock (and Similar Interests).

> (a) *Original Issue.*—On each original issue, whether on organization or reorganization, of shares or certificates of stock, or of profits, or of interests in property or accumulations, by any corporation, or by any investment trust or similar organization (or by any person on behalf of such investment trust or similar organization) holding or dealing in any of the instruments mentioned or described in this subsection or section 1801 (whether or not such investment trust or similar organization constitutes a corporation within the meaning of this title), on each $100 of par or face value or fraction thereof of the certificates issued by such corporation or by such investment trust or similar organization (or of the shares where no certificates were issued), 11 cents: *Provided:* That where such shares or certificates are issued without par or face value, the tax shall be 11 cents per share (corporate share, or investment trust or other organization share, as the case may be),

unless the actual value is in excess of $100 per share; in which case the tax shall be 11 cents on each $100 of actual value or fraction thereof of such certificates (or of the shares where no certificates were issued), or unless the actual value is less than $100 per share, in which case the tax shall be 3 cents on each $20 of actual value, or fraction thereof, of such certificates (or of the shares where no certificates were issued): *Provided further,* That where such certificates (or shares, where no certificates are issued) are issued in a recapitalization, the tax payable shall be that proportion of the tax computed on such certificates or shares issued in the recapitalization that the amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise, bears to the total par value (or actual value if no par stock) of such certificates or shares issued in the recapitalization. The stamps representing the tax imposed by this subsection shall be attached to the stock books or corresponding records of the organization and not to the certificates issued.

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In the Supreme Court of the United States

OCTOBER TERM, 1956

No. 664

UNITED STATES STEEL CORPORATION, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES IN OPPOSITION

OPINION BELOW

The opinion of the Court of Claims (Pet. 13–24) is reported at 142 F. Supp. 948.

JURISDICTION

The judgment of the Court of Claims was entered on June 5, 1956. Petitioner's motion for rehearing was denied on October 2, 1956. The petition for a writ of certiorari was filed on December 28, 1956. The jurisdiction of this Court is invoked under 28 U. S. C., Section 1255 (1).

QUESTIONS PRESENTED

1. Where a corporation reduces the value of its stock from $100 to $75 per share and in the same

year reduces its capital account, whether a proportionate increase in the capital account ten years later out of previously untaxed earned and capital surplus accounts is "dedicated as capital for the first time" and hence taxable under Section 1802 (a) of the Internal Revenue Code of 1939.

2. Whether the dedication of an amount from a corporation's capital and earned surplus accounts to its common stock account which is followed by a stock split and the issuance of additional stock certificates constitutes an original issue of certificates or shares under Section 1802 (a) of the Internal Revenue Code of 1939.

STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of Sections 1800 and 1802 (a) of the Internal Revenue Code of 1939, and of Sections 113.20, 113.23, and 113.25 of Treasury Regulations 71 (1941 ed.), are set forth in the Appendix, *infra*, pp. 9–13.

STATEMENT

The facts, all of which were stipulated by the parties and were found by the Court of Claims (Pet. 24–29), may be summarized as follows:

Petitioner is a corporation organized and existing under the laws of the State of New Jersey. From 1901 to 1931, petitioner issued a total of 8,703,252 shares of common stock, having a par value of $100 per share, and dedicated to its "common stock capital account" the amount of $870,325,200. Documentary stamp taxes were paid by petitioner on these

amounts. Of these shares of common stock, 1,587,017 were issued in 1929, 1930, and 1931, for cash and property having an aggregate book value of $239,951,721.42, or $81,250,021.42 in excess of the par value of such shares. No stamp tax was paid with respect to the $81,250,021.42 excess, and this excess amount was placed on petitioner's books in a capital surplus account. (Pet. 24–26.)

In 1938, petitioner changed its common stock from par value of $100 per share to no par value with a stated value of $75 per share. This resulted in a reduction in the stated value of the common stock then outstanding and in the common stock capital account from $870,325,200 to $652,743,900, or a reduction of $217,581,300. This amount was credited to the capital surplus account and, when added to the $81,250,021.42 already in that account, increased the total capital surplus to $298,831,321.42. (Pet. 26.)

In December, 1938, petitioner reduced the value of some intangible property from $260,368,521.53 to $1, and the sum of $260,368,520.53 was charged against the capital surplus account, reducing the balance in this account to $38,462,800.89. (Pet. 27.)

On January 25, 1949, petitioner's board of directors adopted a resolution to transfer, as of December 31, 1948, the $38,462,801 remaining in the capital surplus account to the common stock capital account, and $179,118,499 from earned surplus to common stock capital account, or a total of $217,581,300. Such transfers were to increase the stated capital outstanding from $75 per share to $100 per share. (Pet. 27.)

At the same meeting of January 25, 1949, the board of directors recommended a three-for-one split in the no par common stock by changing the stated value of each no par share from $100 to $33⅓ per share and thereby increasing the number of shares of common stock outstanding. The stockholders approved this stock split on May 2, 1949, at the first regularly scheduled stockholders' meeting subsequent to the meeting of the board of directors. Pursuant to this action of the board of directors and stockholders, the certificates representing one or more shares of common stock which were issued and outstanding immediately prior to the stock split remained outstanding, and new certificates were issued in June, 1949, representing two additional shares of common stock. (Pet. 27–29.)

The Commissioner assessed a documentary stamp tax upon the entire $217,581,300 transferred to the common stock capital account. Petitioner paid the tax together with interest, or a total of $264,942.19. (Pet. 29.) Thereafter petitioner filed a claim for refund with the District Director of Internal Revenue. After its claim was denied, it filed the instant suit in the Court of Claims.

The Court of Claims held (Pet. 13–20), with one judge dissenting, that the $179,118,499.11 taken out of earned surplus and placed in the capital account, plus $10,457,750.48 of the $38,462,800.89 transferred from the capital surplus account to the common stock capital account, were amounts dedicated as capital for

the first time and were properly taxable.[1] The Court of Claims also held (Pet. 20–21) that the dedication of amounts to capital as of December 31, 1948, which was followed by the issuance of stock in June, 1949, in connection therewith, constitutes an original issue of stock for which a tax may be imposed under Section 1802 (a) of the 1939 Code.

ARGUMENT

1. Section 1802 (a) of the 1939 Code (Appendix *infra*, pp. 9–10) imposes a stamp tax upon each original issue, whether on organization or reorganization, of shares or certificates of stock (or of profits, or of interests in property, or accumulations) by any corporation. If the stock issued has a par value, the tax is imposed upon the par value. If the stock does not have any par, the tax is imposed upon the actual value of the certificates (or of the shares where no certificates were issued). Section 1802 was amended by the Act of August 8, 1947, 61 Stat. 921, which added a provision that, where certificates were issued in a recapitalization, the tax payable on such certificates shall be limited to the "amount dedicated as

[1] In arriving at this figure of $10,457,750.48, the Court took a percentage of the $38,462,800, the balance in petitioner's capital surplus account after the write-down of petitioner's assets in 1938. Originally this account carried $81,250,021.42 which was not taxed. In 1938, taxpayer transferred $217,581,300 to this account which had previously been dedicated as capital and upon which the tax had been paid, making the total amount in the account $298,831,321.42. For this reason, the Court of Claims took 81,250,021.42/298,831,321.42 of the $38,462,800.89 remaining in the capital surplus account to represent the balance remaining in the account which had not previously been taxed.

capital for the first time" by the recapitalization, whether by a transfer of earned surplus or otherwise.

Thus, where funds transferred from a corporation's earned or capital surplus account cannot be shown to have been previously dedicated to capital, it is universally held that they are subject to the stamp tax imposed by Section 1802 (a). *Crown Cork & Seal Co.* v. *United States*, 94 F. Supp. 117 (C. Cls.); *W. T. Grant Co.* v. *Duggan*, 94 F. 2d 859 (C. A. 2d); *United States* v. *Pure Oil Co.*, 135 F. 2d 578 (C. A. 7th); *United States* v. *California Electric Power Co.*, 187 F. 2d 313 (C. A. 9th); Section 113.23 (e) of Treasury Regulations 71 (1941 ed.), as amended by T. D. 5613, 1948–1 Cum. Bull. 133 (Appendix, *infra*, pp. 10–12). Cf. *Crown Zellerbach Corp.* v. *Anglim*, 109 F. Supp. 514 (N. D. Cal.). The decision here is in accord with that well-settled doctrine.

Contrary to petitioner's contention (Pet. 6), there is no conflict between the decision below and the Seventh Circuit decision in *United States* v. *Pure Oil Co.*, *supra*. In this connection, petitioner relies on the statement in *Pure Oil* that "book entries alone are not decisive" in determining taxability. 135 F. 2d at 579. But the decision below is based, not on book entries alone, but rather on what was actually done (rather than, as the petitioner contended, upon what might have been done). (Pet. 17.) The court found, on all the facts, that the $189,576,249.59 transferred by petitioner from its surplus accounts to the capital accounts constituted an "amount dedicated as capital for the first time." The pertinent book entries

do no more than reflect this conclusion. In the *Pure Oil* case, moreover, it was merely held that book entries need not identify the new shares delivered for old where "[t]he undisputed fact is that the old preferred stock was exchanged share for share and the dividend arrears satisfied by issuance of additional shares." 135 F. 2d at 579.

2. Nor does the decision conflict with *American Steel Foundries* v. *Sauber* (C. A. 7th), decided November 27, 1956 (1956 C. C. H., par. 10,081). In that case, the Seventh Circuit held that a mere dedication of surplus to capital, without the issuance of any stock, was not subject to tax under Section 1802 (a). The court below likewise held that both a dedication of capital and the issuance of stock are necessary. The court further held that here the two were in reality parts of a single plan. (Pet. 20.) See *Southern Pac. Co.* v. *Berliner,* 176 F. 2d 671 (C. A. 9th); *Rio Grande Oil Co.* v. *Welch,* 101 F. 2d 454 (C. A. 9th); *W. T. Grant Co.* v. *Duggan, supra; American Gas & Electric Co.* v. *United States,* 69 F. Supp. 614 (S. D. N. Y.).

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CONCLUSION

The decision below is correct. There is no conflict, and the question is not an important one. Accordingly, it is respectfully submitted that the petition for a writ of certiorari should be denied.

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JANUARY, 1957.

APPENDIX

Internal Revenue Code of 1939:

SEC. 1800. IMPOSITION OF TAX.

There shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in sections 1801 to 1807, inclusive, or for or in respect of the vellum, parchment, or paper upon which such instruments, matters, or things, or any of them, are written or printed, the several taxes specified in such sections.

(26 U. S. C., 1952 ed., sec. 1800.)

SEC. 1802. CAPITAL STOCK (AND SIMILAR INTERESTS).

(a) [As amended by Sec. 521 (a) (4), Revenue Act of 1941, c. 412, 55 Stat. 687, and Act of August 8, 1947, c. 518, 61 Stat. 921] *Original Issue.*—On each original issue, whether on organization or reorganization, of shares or certificates of stock, or of profits, or of interests in property or accumulations, by any corporation, or by any investment trust or similar organization (or by any person on behalf of such investment trust or similar organization) holding or dealing in any of the instruments mentioned or described in this subsection or section 1801 (whether or not such investment trust or similar organization constitutes a corporation within the meaning of this title), on each $100 of par or face value or fraction thereof of the certificates issued by such corporation or by such investment trust or similar organization (or of the shares where no certificates were issued), 11 cents: *Provided,* That

where such shares or certificates are issued without par or face value, the tax shall be 11 cents per share (corporate share, or investment trust or other organization share, as the case may be), unless the actual value is in excess of $100 per share; in which case the tax shall be 11 cents on each $100 of actual value or fraction thereof of such certificates (or of the shares where no certificates were issued), or unless the actual value is less than $100 per share, in which case the tax shall be 3 cents on each $20 of actual value, or fraction thereof, of such certificates (or of the shares where no certificates were issued): *Provided further,* That where such certificates (or shares, where no certificates are issued) are issued in a recapitalization, the tax payable shall be that proportion of the tax computed on such certificates or shares issued in the recapitalization that the amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise, bears to the total par value (or actual value if no par stock) of such certificates or shares issued in the recapitalization. The stamps representing the tax imposed by this subsection shall be attached to the stock books or corresponding records of the organization and not to the certificates issued.

(26 U. S. C. 1952 ed., Sec. 1802.)

* * * * *

Treasury Regulations 71 (1941 ed.):

SEC. 113.20 [As amended by T. D. 5613, 1948–1 Cum. Bull. 133]. *Scope of Tax.*—Section 1802 (a) imposes a tax upon each original issue of certificates (or shares when issued without certificates) of stock, or of profits, or of interest in property or accumulations by (1) any corporation, or (2) any investment trust or similar organization (whether or not constituting a

corporation within the meaning of the Internal Revenue Code) holding or dealing in any of the instruments mentioned or described in section 1801 (see Subpart E) or section 1802 (a), or (3) any person (such as a depositary) on behalf of such investment trust or similar organization. The tax applies to each original issue of the shares or certificates specified, irrespective of the purpose of the issue, the person to whom issued, or the time of delivery.

The tax also applies to shares or certificates issued in a recapitalization where the recapitalization results in the dedication of an amount as capital for the first time. However, in the case of shares or certificates so issued on or after August 8, 1947, the tax is subject to the limitation set forth in section 113.23 (e).

SEC. 113.23 [As amended by T. D. 5613, *supra*]. *Rate and Computation of Tax.*—* * *

* * * * *

(e) *Stock issued on or after August 8, 1947, in a recapitalization.*—Where stock is issued on or after August 8, 1947, in a recapitalization, the tax payable is that proportion of the total tax computed with respect to all the shares or certificates so issued that the amount dedicated as capital for the first time by the recapitalization, whether by a transfer of earned surplus or otherwise, bears to the total par value (or actual value if no par stock) of the shares or certificates so issued.

A tax is not payable with respect to stock issued in a recapitalization unless the recapitalization results in the dedication of an amount as capital which amount is so dedicated for the first time. Thus, where a corporation transferred an amount from capital to capital surplus in a prior recapitalization, and such corporation in a subsequent or second recapitalization transfers such amount from capital surplus to capital under such circumstances that

the amount so restored to capital is clearly identifiable, a tax is not payable with respect to the amount so rededicated as capital. However, the tax is payable with respect to a transfer of capital surplus to capital by way of a recapitalization where the amount so transferred had not been previously dedicated as capital.

Where a recapitalization is effected in connection with, or as part of, some other transaction, for example—an original or an additional issue of stock; a merger; etc.—the limitation of the tax payable to the proportion specified in this subsection applies only to the stock issued in that part of the transaction which constitutes a recapitalization. Thus, where a corporation makes a change in its capital structure by replacing an issue of stock with another issue of stock and at the same time disposes of part of the new stock by sale to underwriters, the tax limitation is applicable only to that portion of the new stock which is issued in exchange for the old stock retired thereby. In such case, the portion of the new stock sold to the underwriters is taxable in its entirety without any adjustment on account of the recapitalization. Similarly, where a corporation retires its preferred stock by issuing common stock in exchange therefor, and such exchange is made in connection with a merger in which the corporation issues common stock also to the former stockholders of the merged company, the tax limitation is applicable only to the common stock issued in exchange for the preferred stock, and the shares or certificates of common stock issued to the former stockholders of the merged company are subject to tax without any adjustment on account of the recapitalization.

SEC. 113.25. *Issues Not Subject to Tax.*—In addition to the various issues specifically ex-

empt under section 1808, as to which see Subpart J, the following are examples of issues not subject to the tax:

* * * * *

(f) The issue of stock in a recapitalization or reorganization where there is no dedication of additional capital, either by transfer of earned surplus or otherwise.

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